Monday, 15 May 2023

RBA Eyeing Jobs and Wages

The past two weeks have been crazy for economists and markets. A line-ball Reserve Bank (RBA) meeting, which ultimately wrong-footed markets and most forecasters and the ever-important Federal Budget - which is still being fully unpacked. Add in there a treasure trove of economic data and there's not much more an economist could want.

This week doesn't disappoint either. Given the current economic environment the RBA is never far from the fray, and they will again be in the spotlight this week as we receive the minutes from the May Board meeting and key data on wages and the labour market.

The RBA's May meeting was no routine affair. A pause in April left many thinking that an upside data surprise was needed for the RBA to resume hiking. And the data coming into the meeting didn't raise any eyebrows. Market pricing had basically ruled out the chance of a hike, and most economists had another pause as their 'central scenario' – but we underscored that the decision remained finely balanced. In the event, the RBA opted to hike the cash rate by 25 basis points. The policy statement and remarks from Governor Lowe in a speech following the decision suggest it was the balance of risks that tipped the Board in favour of a hike. While the inter-meeting data evolved broadly in-line with the RBA's implied trajectory, the Board perceived that the risk inflation would be too slow to return to target remained too high. Higher asset prices, including a bottoming in the dwelling price cycle and prices starting to increase again, were also noted by Governor Lowe in his speech. Tomorrow, the meeting minutes will give us a deeper glimpse into the factors driving the Board's decision and a more detailed account of what they will be looking for come future meetings.

Wages growth and relatedly, the labour market, will no doubt be on that list. The RBA's progress on inflation will be a key input into coming policy decisions, and this progress is being driven by two contrasting dynamics. A normalisation in goods prices as disruptions from the pandemic and the invasion of Ukraine wash through the numbers, partly offset by an acceleration in services inflation as the tight labour market translates into firmer wages growth.

Guarding against the risk that the pace of wages growth becomes inconsistent with the forecast return to the 2-3% inflation target band is a key objective of the RBA. The Board has noted that while aggregate wages growth to-date is not inconsistent with a return to the inflation target, they remain vigilant of this risk given the incredibly tight labour market. When the wage price index (WPI) is released on Wednesday, we are expecting to see a further acceleration in the annual pace of wages growth. We see the WPI growing at 3.5% over the year to the March quarter, up from 3.3% at the end of 2022. But we expect quarterly growth to hold steady at 0.8%. While annual growth is expected to accelerate, a stagnation in quarterly growth, if realised, will point to a stabilisation in wage-pressures. This will be a welcome sign for the RBA and a further sign that wage pressures remain in-check.

The forecast stabilisation in wage pressures is a product of a changing labour market. Conditions in the jobs market are still exceptionally tight but we have started to see an easing in conditions at the margins as the supply of labour comes back online at a record pace. As the gap between labour demand and supply closes, we expect to see a further increase in employment as businesses find it easier to hire staff and the long list of open positions is filled. In April, we expect that this increase in employment amounted to 40.0k, a very solid number. A tick up in the participation rate to 66.8% is anticipated to see the unemployment rate hold unchanged at 3.5%. If realised, this would represent a very strong set of numbers, but the RBA will also be interested in how quickly labour supply is expanding. In particular, growth in the working-age population and the size of the labour force.

At this stage, we think the RBA will go on pause again in June and leave the cash rate unchanged at 3.85% for the remainder of the year. However, there is a risk that additional tightening in monetary policy may be necessary. Given the importance of the labour market and wages to inflation, and specifically services inflation, any surprise strength in the data will increase that risk.

Jameson Coombs, Economist
Ph: +61 401 102 789

Group Forecasts

		2023			2024		
End Period:	**Close (12 May)**	**Q2 (f)**	**Q3 (f)**	**Q4 (f)**	**Q1 (f)**	**Q2 (f)**	**Q3 (f)**
Aust. Interest Rates:							
RBA Cash Rate, %	3.85	3.85	3.85	3.85	3.60	3.35	3.10
90 Day BBSW, %	3.89	3.95	3.95	3.97	3.72	3.47	3.22
3 Year Swap, %	3.45	3.60	3.50	3.40	3.30	3.10	2.90
10 Year Bond, %	3.32	3.40	3.30	3.20	3.00	2.80	2.70
US Interest Rates:							
Fed Funds Rate, %	5.125	5.125	5.125	4.875	4.375	3.875	3.375
US 10 Year Bond, %	3.46	3.50	3.40	3.30	3.10	2.90	2.80
USD Exchange Rates:							
AUD-USD	0.6646	0.69	0.72	0.74	0.75	0.76	0.76
USD-JPY	135.70	132	130	128	127	126	125
EUR-USD	1.0849	1.11	1.11	1.12	1.13	1.14	1.15
GBP-USD	1.2458	1.25	1.25	1.26	1.26	1.27	1.28
NZD-USD	0.6193	0.64	0.66	0.67	0.68	0.68	0.68
AUD Exchange Rates:							
AUD-USD	0.6646	0.69	0.72	0.74	0.75	0.76	0.76
AUD-EUR	0.6122	0.62	0.65	0.66	0.67	0.67	0.66
AUD-JPY	90.154	91.1	93.6	94.7	95.3	95.8	95.0
AUD-GBP	0.5335	0.55	0.58	0.59	0.60	0.60	0.59
AUD-NZD	1.0739	1.08	1.09	1.10	1.11	1.13	1.13

	2021	**2022**	**2023 (f)**	**2024 (f)**
GDP, %	4.6	2.7	1.0	1.5
CPI (Headline), %	3.5	7.8	4.0	3.1
CPI (Trimmed mean), %	2.7	6.9	3.7	3.1
Unemployment Rate, %	4.7	3.5	4.5	5.0
Wages Growth, %	2.4	3.3	4.0	3.2

AUD cross exchange rates have been rounded.

Financial forecasts are quarter end.

GDP, CPI, employment and wage growth forecasts are year end.

Contact Listing

Chief Economist
Besa Deda
dedab@stgeorge.com.au
+61 404 844 817

Senior Economist
Pat Bustamante
pat.bustamante@stgeorge.com.au
+61 468 571 786

Senior Economist
Jarek Kowcza
jarek.kowcza@stgeorge.com.au
+61 481 476 436

Economist
Jameson Coombs
jameson.cooombs@stgeorge.com.au
+61 401 102 789